APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT DATED APRIL 13, 2004

UNITED STATES COURT OF APPEALS
For the First Circuit

No. 03-1321

IN RE BANK OF NEW ENGLAND CORP.,

Debtor.

HSBC BANK USA AND JPMORGAN CHASE BANK,
AS INDENTURE TRUSTEES,

Appellants,

v.

DR. BEN S. BRANCH,
TRUSTEE IN BANKRUPTCY, ET AL.,

Appellees.

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

[Hon. Richard G. Stearns, *U.S. District Judge*]
[Hon. William C. Hillman, *U.S. Bankruptcy Judge*]

Appendix A

Before

Selya, *Circuit Judge*,
Coffin, *Senior Circuit Judge*,
and Smith,* *District Judge*.

April 13, 2004

SELYA, *Circuit Judge*. This is a case that straddles a crossroads formed by the intersection of federal and state law. It requires us to decide an issue of first impression in this circuit regarding the enforceability in bankruptcy of agreements that allow the subordination of certain indebtedness. Our decision partially contradicts the decision of the only other court of appeals to have grappled with this same set of questions, *see Chem. Bank v. First Trust of N.Y.* (*In re Southeast Banking Corp.*), 156 F.3d 1114 (11th Cir. 1998), and to that extent creates a circuit split.

The precise dispute between the parties focuses on the priority (if any) that attaches to payment of post-petition interest on indebtedness that benefits from the contractual subordination of other indebtedness. As the question has been framed by the litigants and the lower courts, the answer depends on whether the subordination provisions at issue comply with the Rule of Explicitness. So phrased, the question assumes the continued vitality of that rule. Because we doubt the accuracy of that assumption, we step back to the beginning and inquire into the basis for believing that the Rule of Explicitness remains alive and well.

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* Of the District of Rhode Island, sitting by designation.

That step places us at the head of a long and winding path. After traveling it, we conclude that the enactment of section 510(a) of the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, 2586 (codified at 11 U.S.C. § 510(a)), extinguished the Rule of Explicitness in its classic form. We further conclude that states are not free to adopt rules of contract interpretation that apply only in bankruptcy. For purposes of this case, then, the Rule of Explicitness is a dead letter.

Faced with this reality, we proceed to analyze the effect of the subordination provisions under New York's generally applicable principles of contract law—principles that do not embody any canon that operates in the same manner as the Rule of Explicitness. That analysis reveals an ambiguity in the language of the subordination provisions. The resolution of this ambiguity requires an inquiry into the parties' intent. That inquiry is fact-based and the bankruptcy court has not made the necessary findings. Consequently, we vacate the judgment below and remand for further proceedings.

I. BACKGROUND

The underlying facts are largely undisputed. In its halcyon days, the Bank of New England (BONE) issued six separate series of debt instruments.[1] Clearly worded choice of law provisions tie the construction and interpretation of these instruments to the law of New York. Three of these offerings (the Senior Debt) are entitled to the benefit of

1. Two of these were actually issued by BONE's predecessors in interest, but this technicality in no way affects our analysis. Thus, we disregard it.

contractual subordination provisions. They include (i) a series of debentures bearing interest at 7.625% per annum, due in 1998, in the aggregate principal amount of $25,000,000; (ii) a series of debentures bearing interest at 8.85% per annum, due in 1999, in the aggregate principal amount of $20,000,000; and (iii) a series of notes bearing interest at a rate of 9.5% per annum, due in 1996, in the aggregate principal amount of $150,000,000. HSBC Bank USA and JPMorgan Chase Bank, appellants here, serve as Indenture Trustees for the Senior Debt. The remaining three offerings (the Junior Debt) are subordinated to the Senior Debt. They include (i) a series of floating rate debentures, due in 1996, in the aggregate principal amount of $75,000,000; (ii) a series of debentures bearing interest at 8.75% per annum, due in 1999, in the aggregate principal amount of $200,000,000; and (iii) a series of debentures bearing interest at 9.875% per annum, due in 1999, in the aggregate principal amount of $250,000,000. Each trust indenture referable to Junior Debt contains a subordination provision that is substantially similar to the following:

> [E]ach Holder likewise covenants and agrees by his acceptance thereof, that the obligations of the Company to make any payment on account of the principal of and interest on each and all of the Notes shall be subordinate and junior, to the extent and in the manner hereinafter set forth, in right of payment to the Company's obligations to the holders of Senior indebtedness of the Company.

Each of these indentures also specifies that:

Appendix A

> The Company agrees that upon . . . any payment or distribution of assets of the Company of any kind or character, whether in cash, property or securities, to creditors upon any dissolution or winding up or total or partial liquidation or reorganization of the Company, whether voluntary or involuntary or in bankruptcy, insolvency, receivership, conservatorship or other proceedings, all principal (and premium, if any), sinking fund payments and interest due or to become due upon all Senior Indebtedness of the Company shall first be paid in full, or payment thereof provided for in money or money's worth in accordance with its terms, before any payment is made on account of the principal of or interest on the indebtedness evidenced by the [Junior] Notes due and owing at the time. . . .

On January 7, 1991, BONE filed a voluntary petition for bankruptcy. *See* 11 U.S.C. §§ 701-766. At that time, much of the Senior and Junior Debt was still outstanding. Everyone agrees that, in bankruptcy, the holders of the Senior Debt are contractually entitled to priority. Withal, the parties fiercely dispute whether that priority extends to the payment of post-petition interest.

Since filing for bankruptcy, BONE, under the careful stewardship of its Chapter 7 trustee, has made three distributions to creditors. Through these distributions, the bankruptcy estate has paid the holders of the Senior Debt the full amount of all unpaid principal and pre-petition interest, together with all approved fees and expenses

incurred through the date of the last distribution (October 26, 1999). The trustee then created an ample reserve for future fees and expenses and, at that point, concluded that he had satisfied the obligations owed to the holders of the Senior Debt. When, thereafter, the trustee determined that there existed sufficient unencumbered funds, he sought permission to make a distribution in the amount of $11,000,000 to the holders of the Junior Debt. The appellants objected on the ground that the trustee had not yet paid post-petition interest on the Senior Debt.

The bankruptcy court overruled this objection and authorized the proposed distribution. *In re Bank of New Engl. Corp.*, 269 B.R. 82, 86 (Bankr. D. Mass. 2001). The court based its decision on the Rule of Explicitness, holding that New York law recognized the rule and that the language of the subordination provisions failed to satisfy it. *Id.* at 85-86. The district court affirmed. *HSBC Bank USA v. Bank of New Engl. Corp. (In re Bank of New Engl. Corp.)*, 295 B.R. 419, 424-25 (D. Mass. 2003). The court's analysis differed somewhat from that of the bankruptcy court, but it too deemed the Rule of Explicitness controlling. *Id.* at 424. This appeal ensued.

II. DISCUSSION

We cede no special deference to the district court's initial review of the bankruptcy court's decision. *See Gannett v. Carp (In re Carp)*, 340 F.3d 15, 21 (1st Cir. 2003). Rather, we look directly to the bankruptcy court's decision, examining that court's findings of fact for clear error and its conclusions of law de novo. *Id.* Insofar as the bankruptcy

court's decision hinges on an interpretation of the Bankruptcy Code, it presents a question of law (and, thus, engenders de novo review). *United States v. Yellin (In re Weinstein)*, 272 F.3d 39, 42 (1st Cir. 2001).

As the litigants and the lower courts have framed the issue, the pivotal question is whether the language of the subordination provisions satisfies the Rule of Explicitness. We do not agree that this is the correct question. Thus, we retreat to first principles.

Subordination agreements are essentially inter-creditor arrangements. 4 Lawrence P. King et al., Collier on Bankruptcy ¶ 510.03[2], at 510-7 (15th rev. ed. 2003). They are designed to operate in a wide range of contingencies, one of which is insolvency. As a hedge against the ravages of a future bankruptcy, subordination agreements typically provide that one creditor will subordinate its claim against the debtor (the putative bankrupt) in favor of the claim of another creditor. This subordination alters the normal priority of the junior creditor's claim so that it becomes eligible to receive a distribution only after the claims of the senior creditor have been satisfied. *Id.* at ¶ 510.01, at 510-3.

Prior to 1978, the Bankruptcy Act contained no specific mention of subordination agreements. *See* Alan N. Resnick & Brad Eric Scheler, *The Right of a Senior Creditor to Receive Post-Petition Interest from a Subordinated Creditor's Distributions: Did the Rule of Explicitness Survive the Enactment of the Bankruptcy Code?*, 32 Uniform Comm. Code L.J. 466, 466 (2000). Accordingly, subordination provisions were enforced in bankruptcy through the bankruptcy court's

equitable powers. *See, e.g., Bankers Life Co. v. Mfrs. Hanover Trust Co. (In re Kingsboro Mortg. Corp.)*, 514 F.2d 400, 401-02 (2d Cir. 1975) (per curiam); *Matter of Time Sales Fin. Corp.*, 491 F.2d 841, 844 (3d Cir. 1974); *Bird & Sons Sales Corp. v. Tobin*, 78 F.2d 371, 373 (8th Cir. 1935). Enforcing such agreements was necessary to prevent junior creditors from receiving windfalls after having explicitly agreed to accept less lucrative payment arrangements. *See Matter of Credit Indus. Corp.*, 366 F.2d 402, 410 (2d Cir. 1966); *In re Hinderliter Indus., Inc.*, 228 B.R. 848, 853 (Bankr. E.D. Tex. 1999). Equity dictated enforcement because "[e]quality among creditors who have lawfully bargained for different treatment is not equity but its opposite." *Chem. Bank N.Y. Trust Co. v. Kheel*, 369 F.2d 845, 848 (2d Cir. 1966).

Defining the outer limits of this equitable rule, especially with respect to post-petition interest, posed a thorny problem. Generally, the accrual of interest on an unsecured or undersecured claim stops upon the debtor's filing of a bankruptcy petition. *See, e.g., Nicholas v. United States*, 384 U.S. 678, 682 (1966); *Sexton v. Dreyfus*, 219 U.S. 339, 344 (1911); *see also* 11 U.S.C. § 502(b)(2); Bankruptcy Act of 1898, § 63(a). Yet, subordination agreements sometimes contain language that prioritizes (or, at least, arguably prioritizes) the payment of post-petition interest on senior indebtedness over any recovery on junior indebtedness. From the outset, courts have been uncomfortable with enforcing this type of prioritization for fear that cases would arise "where a senior creditor may potentially recover more under a subordination agreement than its allowable claim against the estate." 4 Collier on Bankruptcy, *supra* ¶ 510.03[3], at 510-8.

To ease this discomfiture, judges fashioned an equitable doctrine to deal with (and, essentially, limit) the prioritization of post-petition interest payments. *See* Resnick & Scheler, *supra* at 467-68. In its simplest form, this equitable doctrine, called the Rule of Explicitness, required that a subordination agreement show clearly "that the general rule that interest stops on the date of the filing of the petition is to be suspended." *Time Sales*, 491 F.2d at 844. Over time, this evolved into a requirement that only unequivocal language could overcome the generic bar on recovery of post-petition interest.

That was the state of the law when Congress enacted the Bankruptcy Code in 1978. Pub. L. No. 95-958, 92 Stat. 2549. Unlike the earlier Bankruptcy Act, the Code deals explicitly with subordination agreements. Section 510(a) provides that a subordination agreement is enforceable in bankruptcy to the same extent as under "applicable nonbankruptcy law." 11 U.S.C. § 510(a). This statutory provision supplants the judge-made doctrine through which the courts previously had dealt with such agreements. Because equitable powers possessed by bankruptcy courts "must and can only be exercised within the confines of the Bankruptcy Code," *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988), the enactment of section 510(a) means that the enforcement of subordination provisions is no longer a matter committed to the bankruptcy courts' notions of what may (or may not) be equitable. *First Fid. Bank v. Midlantic Nat'l Bank (In re Ionosphere Clubs, Inc.)*, 134 B.R. 528, 533 (Bankr. S.D.N.Y. 1991).

That Congress cabined the bankruptcy courts' equitable powers while providing an alternate means for preserving the viability of subordination agreements does not resolve the further question of whether the Rule of Explicitness, through some other medium, survived the enactment of section 510(a). To answer that query, we begin, as always, with the text of the relevant statute. *See 229 Main St. Ltd. P'ship v. Mass. Dep't of Envtl. Prot. (In re 229 Main St. Ltd. P'ship)*, 262 F.3d 1, 5 (1st Cir. 2001). We are mindful, of course, that the language of an unambiguous statute normally determines its meaning. *Id.*

In terms, section 510(a) provides that a "subordination agreement is enforceable in a [bankruptcy] case . . . to the same extent that such agreement is enforceable under applicable nonbankruptcy law." 11 U.S.C. § 510(a). It is clear beyond peradventure that the phrase "applicable nonbankruptcy law" can refer to either federal or state law. *See Patterson v. Shumate*, 504 U.S. 753, 757-59 (1992). Since the construction of private contracts is usually a matter committed to state law, *Volt Info. Scis., Inc. v. Bd. of Trs.*, 489 U.S. 468, 474 (1989), the presumption is that state law will furnish the proper benchmark. That presumption is especially robust here because we can find no federal statute that might guide us in interpreting subordination agreements. *Accord Southeast Banking*, 156 F.3d at 1121.

Of course, it might be possible to argue for the use of federal common law in this context. But resort to a federal common law of contract enforcement ordinarily is justified only when required by a distinct national policy or interest. *See Bartsch v. Metro-Goldwyn-Mayer, Inc.*, 391 F.2d 150,

153 (2d Cir. 1968). The interpretation and enforcement of financial arrangements between private parties does not fill that bill. *See Southeast Banking*, 156 F.3d at 1121 n.8.

To be sure, there is an important federal interest in the uniform application of the bankruptcy law—but that interest will not suffice in this instance to justify resort to federal common law. By requiring that the enforceability of subordination agreements be subject to applicable nonbankruptcy law, Congress determined that such agreements should be interpreted using non-uniform principles. It is not our province to second-guess this determination. To cinch matters, the Supreme Court has instructed us that in the absence of specific statutory provisions to the contrary, property interests should not be analyzed differently as a result of a party's involvement in a bankruptcy case. *Butner v. United States*, 440 U.S. 48, 55 (1979). We take this to mean that bankruptcy courts should only modify the usual state-law compendium of rights and remedies if and to the extent that such modifications are specifically authorized or directed by the Bankruptcy Code.

For these reasons, we conclude that the applicable nonbankruptcy law referred to in *section 510(a)* is state law (and, particularly, state contract law). *Accord In re Best Prods. Co.*, 168 B.R. 35, 69 (Bankr. S.D.N.Y. 1994); 9E Am. Jur. 2d Bankr. § 3113 (2000). It follows inexorably that if the Rule of Explicitness retains any vitality, it does so only as part and parcel of state law. *See* 4 Collier on Bankruptcy, *supra* ¶ 510.03[3], at 510-9, 10 ("[T]he Rule of Explicitness cannot be found in the Code, but resort must be had to the state law governing the contractual subordination agreement."); *see also Southeast Banking*, 156 F.3d at 1124.

This brings us to the parameters of the authority delegated by section 510(a). One thing seems very clear: in keeping with the principle that bankruptcy is an area of distinct federal competence, Congress has conferred on the federal courts the power to apply any and all generally applicable state rules of contract interpretation in construing subordination agreements. But section 510(a) does not vest in the states any power to make bankruptcy-specific rules: the statute's clear directive for the use of applicable *nonbankruptcy* law leaves no room for state legislatures or state courts to create special rules pertaining strictly and solely to bankruptcy matters. *See In re Cross*, 255 B.R. 25, 34 n.5 (Bankr. N.D. Ind. 2000); *cf. Int'l Shoe Co. v. Pinkus*, 278 U.S. 261, 265 (1929) (clarifying that states are not free to enact laws that interfere with federal bankruptcy law or that provide additional or auxiliary regulation with respect to bankruptcy matters).

Formulation of the bankruptcy law requires Congress carefully to balance competing considerations. That effort is manifest here. On the one hand, bankruptcy highly values equitable distribution that is in line with the priorities embodied in the Code itself. On the other hand, equity typically operates to enforce voluntarily bargained-for positions (some of which may contradict the Code's normal priorities). Section 510(a) encapsulates Congress's reconciliation of this conflict. A state's creation of a bankruptcy-only rule of enforcement would outstrip the authority that Congress conferred (and, thus, upset the equilibrium that section 510(a) was designed to achieve). We conclude, therefore, that such a course is not open to the states.

If the Rule of Explicitness is an interpretive principle unique to bankruptcy, it offends this principle. *See Ionosphere Clubs*, 134 B.R. at 533 (suggesting that the old Rule of Explicitness cases may "be inconsistent with the Code's new mandate that subordination provisions be enforceable in bankruptcy to the same extent that they are enforceable under nonbankruptcy law"). A contrary holding—one that allowed a state to adopt a bankruptcy-only Rule of Explicitness—would require certain contractual provisions (those arguably entitling senior noteholders to the payment of interest becoming due at future dates) to achieve a heightened degree of clarity only if the effort to enforce them arose in bankruptcy rather than in some other context. Such a holding would go well beyond the intended reach of section 510(a).

The short of it is that the enforceability of subordination agreements in bankruptcy must be judged by reference to generally applicable state contract law. As it pertains here, this holding limits our consideration to the general principles of New York contract law. If—and only if—the Rule of Explicitness is such a general principle can it be given effect in this case.

The New York courts do not appear to have developed any rules of interpretation that apply specifically to subordination agreements. *See Best Prods.*, 168 B.R. at 69-70; *see also Finest Invs. v. Sec. Trust Co.*, 468 N.Y.S.2d 256, 258 (N.Y. Sup. Ct. 1983) (applying generic rules of construction to subordination clause); *cf.* N.Y.U.C.C. § 1-209 off'l cmt. 4 (stating that the "enforcement of subordination agreements is largely left to supplementary principles under Section 1-103," which codifies the application of the general law of contracts). Moreover, reported decisions from the New York state courts reveal only a

single mention of the Rule of Explicitness. *See Chem. Bank v. First Trust of N.Y. (In re Southeast Banking Corp.)*, 710 N.E.2d 1083, 1084-88 (1999) (a case which, for reasons that we shortly shall explain, does not help our inquiry). Although we are in something of an epistemological quandary—it is always difficult to prove a negative—the near-total absence of authority is compelling proof that the Rule of Explicitness is not part of New York's general contract law.

The decision in *Chemical Bank* does not alter this conclusion. The opinion in that case was a response to a question certified by the United States Court of Appeals for the Eleventh Circuit. Faced with the issue we confront today, that is, whether a subordination provision permitted the payment of post-petition interest ahead of junior indebtedness, the Eleventh Circuit certified the following question to the New York Court of Appeals: "What, if any, language does New York law require in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of the senior creditor's post-petition interest?" *Southeast Banking*, 156 F.3d at 1125. In so doing, the Eleventh Circuit invited the state court to fashion a bankruptcy-specific rule—and it did so without any evidence that New York had incorporated anything resembling the Rule of Explicitness into its general law of contracts.

Having received the invitation, the New York Court of Appeals responded in kind. The court recognized that it was being asked to determine if New York should adopt the Rule of Explicitness as a "guiding interpretive principle of State contract dispute resolution" in bankruptcy cases. *Chem. Bank*, 710 N.E.2d at 1086. The court proceeded to embrace the rule

as a rule of construction *applicable only in bankruptcy. See id.* at 1088 ("In accordance with the Rule of Explicitness, New York law would require specific language in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of allowing the payment of a senior creditor's post-petition interest demand."). The specificity of the court's holding is apparent from its use of the term "post-petition interest"—a term of art applicable only in bankruptcy. We recognize that the *Chemical Bank* court was constrained by the Eleventh Circuit's statement of the certified question. But this constraint does not alter the fact that, in its holding, *Chemical Bank* announced a bankruptcy-only principle. Nothing in that decision persuades us that the Rule of Explicitness is otherwise a part of the armamentarium of interpretive principles generally available to the courts under New York law.

This illustrates our area of disagreement with the Eleventh Circuit. As framed, the question that it put to the New York court was beyond that court's competence to answer. While a federal court must defer when the highest court of a state interprets the state's general contract law, *see, e.g., Daigle v. Me. Med. Ctr., Inc.*, 14 F.3d 684, 689 (1st Cir. 1994), no such deference is due to a state court's importation of a bankruptcy-specific rule into its own jurisprudence.[2]

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2. Although state courts do have the power to interpret federal law, that is not what the New York Court of Appeals was asked to do. The Eleventh Circuit requested the New York court to enunciate a bankruptcy-specific principle of state law. *See Southeast Banking*, 156 F.3d at 1125-26.

That ends this aspect of our inquiry. There is simply no reason to believe that the New York courts would apply the Rule of Explicitness outside the bankruptcy context. Accordingly, the Rule of Explicitness cannot hold sway. To find otherwise would do violence to the language of section 510(a) and set state and federal law on a collision course.

Let us be perfectly clear. If a state, as part of its general contract law, enunciates an interpretive principle that applies to subordination agreements generally (e.g., "construe all subordination provisions strictly and enforce them only if the intent to subordinate is, on a particular set of facts, super-clear"), that principle would be enforceable under section 510(a).[3] In that event, rejecting the prioritization of post-petition interest in the absence of explicit language would be consistent with the general law of the state. Such a situation would not pose the same problem as does a state rule that applies only in bankruptcy.

We acknowledge that this conclusion compels us to part ways with the Eleventh Circuit. We are always reluctant to foment a circuit split, but we have no principled alternative here. The *Southeast Banking* court invited the New York Court of Appeals to craft a special bankruptcy-only canon of contract interpretation. *See* 156 F.3d at 1125. In our view,

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3. We recognize that the source of such an interpretive principle may be a state statute, a canon of construction enunciated by the state courts, or a rule of equity consistently applied. A bankruptcy court's adoption and enforcement of a state equitable principle is not the exercise of the bankruptcy court's own equitable powers, but, rather, an application of state law (and, thus, is a proper exercise of the authority conferred by section 510(a)).

that course of action misapprehends the reach and breadth of section 510(a).

We now proceed to apply New York's general principles of contract enforcement to the facts at hand. This exercise will allow us to ascertain the effect of the provisions at issue upon the post-petition interest priority claimed by the appellants. Typically, the first step is to determine whether the challenged provisions are subordination agreements within the meaning of section 510(a). 4 Collier on Bankruptcy, *supra* ¶ 510.03[2], at 510-7. That step is a formality here: these are subordination clauses, pure and simple.

We next must determine the meaning and effect of the subordination provisions. Initially, we ask whether the provisions are ambiguous with respect to the relative priority of the payment of post-petition interest on the Senior Debt. This is a question of New York law. *See W.W.W. Assocs., Inc. v. Giancontieri*, 566 N.E.2d 639, 642 (1990). The New York Court of Appeals has provided us with clear, if conventional, guidelines:

> Contracts are not to be interpreted by giving a strict and rigid meaning to general words or expressions without regard to the surrounding circumstances or the apparent purpose which the parties sought to accomplish. The court should examine the entire contract and consider the relation of the parties and the circumstances under which it was executed. Particular words should be considered, not as if isolated from the context,

> but in the light of the obligation as a whole and the intention of the parties as manifested thereby. Form should not prevail over substance, and a sensible meaning of words should be sought.

William C. Atwater & Co. v. Panama R. Co., 159 N.E. 418, 419 (1927) (citations and internal quotation marks omitted).

We take it as a given that a contract is ambiguous when its provisions are susceptible of two or more reasonable interpretations. *See Breed v. Ins. Co. of N. Am.*, 385 N.E.2d 1280, 1282 (1978); *Yanuck v. Simon Paston & Sons Agency, Inc.*, 618 N.Y.S.2d 295, 296 (N.Y. Sup. Ct. 1994). That is the case here. Although each word, taken in isolation, may have a reasonably definite meaning, we must examine these words collectively. *See Atwater*, 159 N.E. at 419. When we do, ambiguity surfaces.

The pertinent language requires full payment of "interest due or to become due" upon the occurrence of a number of events (including bankruptcy, insolvency, receivership, conservatorship, or "other proceedings"). The meaning of "interest due or to become due" seems obvious in the context of, say, a municipal bond: upon the occurrence of a triggering event, interest that has been earned but is not yet due to be paid becomes entitled to a priority.[4] Thus, the application of this group of words in the context of most triggering events is fairly straightforward. But bankruptcy—an event

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4. We provide an example. If interest accruing on a bond is paid every six months (e.g., February 1 and August 1) and a triggering event occurs on May 1, the contractual language provides that all interest earned from February 1 through May 1 is entitled to prioritization (even though that interest is not yet due).

specifically referenced in the subordination provisions—alters the equation. Bankruptcy provides a special system of legal rules that occupies the field upon the filing of a petition. One byproduct of this special set of rules is that all interest is considered due as of the filing date. *See* 11 U.S.C. §§ 101(5)(a), 502(b). Conversely, interest that normally would accrue after that date is generally not recoverable at all (at least, not recoverable from the debtor). *See id.* § 502(b)(2).

These special rules cloud the meaning of the phrase "interest due or to become due." On the one hand, those words reasonably can be interpreted to apply only to triggering events outside of the bankruptcy context (where they have an unambiguous meaning). On the other hand, those words reasonably can be interpreted—as the appellants exhort—to apply to all triggering events, including bankruptcy. In that context, however, the words have no clear meaning and a court faces further ambiguity in trying to determine their contours. After all, in most cases the phrase "due or to become due" simply refers to unmatured interest. At the time of a bankruptcy filing, however, there is no unmatured interest, so the clause may be interpreted either to carry the same "nonbankruptcy" meaning throughout or to take on a bankruptcy-specific meaning (which would cover post-petition interest). Because each of these interpretations seems plausible, we believe that the subordination provisions—as they apply in bankruptcy—are ambiguous. *Cf. Southeast Banking*, 156 F.3d at 1124 (finding the phrase "paid in full" ambiguous *in the context of bankruptcy proceedings*).

In fine, we find the words "due or to become due" lacking in certitude as to whether they actually provide for the payment of post-petition interest on the Senior Debt prior to any payment referable to the Junior Debt. New York law requires that this

amphiboly be resolved through a contextual examination of the parties' intent, taking full account of the surrounding facts and circumstances. *Ruttenberg v. Davidge Data Sys. Corp.*, 626 N.Y.S.2d 174, 178 (N.Y. Sup. Ct. 1995); *Yanuck*, 618 N.Y.S.2d at 296; *Tobin v. Union News Co.*, 239 N.Y.S.2d 22, 25 (N.Y. Sup. Ct. 1963). Discerning this intent ordinarily requires the adjudication of factual questions. *See Ruttenberg*, 626 N.Y.S.2d at 175; *Yanuck*, 618 N.Y.S.2d at 296; *see also Time Warner Entm't Co. v. Brustowsky*, 634 N.Y.S.2d 82, 82 (N.Y. Sup. Ct. 1995) (noting that factfinding generally will be necessary if the contract term at issue is "susceptible to varying reasonable interpretations"). A trial can be avoided only if the parties' intent is made manifest within the four corners of the contract itself. *Ruttenberg*, 626 N.Y.S.2d at 175-76.

In the case at bar, it is impossible to glean the parties' intent from the language and structure of the instruments alone. These documents evidence complex commercial transactions, and the matter is further complicated because the beneficiaries of the subordination provisions—the holders of the Senior Debt—are not parties to the agreements containing the subordination provisions (those agreements are directly appurtenant to the Junior Debt). Given these realities, we are persuaded that resolution of the intent question cannot be accomplished by the simple expedient of examining the relevant paperwork, but, rather, requires differential factfinding.[5] Because the bankruptcy

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5. To be sure, the backdrop of bankruptcy may inform the examination into the parties' intent. *See Dolman v. U.S. Trust Co.*, 157 N.Y.S.2d 537, 541-42 (N.Y. Sup. Ct. 1956) (noting the presumption "that the parties had [the law in force at the time of agreement] in contemplation when the contract was made," and that

(Cont'd)

court has not yet developed a record with this inquiry in mind, we remand for factfinding on the parties' intent vis-à-vis post-petition interest.

III. CONCLUSION

We need go no further. We hold that the Rule of Explicitness has no application in the context of bankruptcy where, as here, the state has not adopted the rule as one of general applicability. Consequently, we turn to generic principles of state law to interpret the contractual provisions at issue. Applying those principles, we find the subordination provisions ambiguous as to whether they provide for the priority payment of post-petition interest. This finding necessitates an examination into the intent of the parties—an inquiry which, in the circumstances of this case, entails questions of fact that must in the first instance be addressed by the bankruptcy court. We therefore vacate the decision of the district court and remand with instructions that the district court vacate the judgment of the bankruptcy court and remand the matter to that tribunal for further proceedings consistent with this opinion.

Vacated and remanded. All parties shall bear their own costs.

(Cont'd)

the contract generally will be "construed in light of such law"). Here, however, the effect of that tenet is uncertain absent further factfinding. *Cf. Time Warner Entm't*, 634 N.Y.S.2d at 83 (finding a regulatory definition of a term not determinative of its meaning in a contract where proof was adduced indicating that the parties intended an independent meaning).

APPENDIX B — OPINION OF THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF MASSACHUSETTS DATED FEBRUARY 3, 2003

UNITED STATES DISTRICT COURT
DISTRICT OF MASSACHUSETTS

CIVIL ACTION NUMBER 01-12229-RGS

IN RE:

BANK OF NEW ENGLAND CORPORATION,

Debtor.

HSBC BANK USA, AS INDENTURE TRUSTEE, AND JP MORGAN CHASE BANK f/k/a THE CHASE MANHATTAN BANK, AS INDENTURE TRUSTEE,

Appellants

v.

BANK OF NEW ENGLAND CORPORATION,

Appellee

February 3, 2003

STEARNS, D.J.

On December 17, 2001, the Senior Debt holders of the bankrupt Bank of New England Corporation (BNEC), appealed a November 1, 2001 order of the Bankruptcy Court authorizing a distribution of assets from BNEC's estate to

the Junior Debt holders. Appellants maintain that no such distribution can be made before they are paid post-petition interest.

Prior to BNEC's spectacular collapse, it obligated itself to six separate issues of Indenture debt, totaling $705,972,000. Under the terms of the Indentures, the first three issues (the Senior Debt) were to have priority over the remaining three issues (the Junior Debt). Each of the Junior Debt Indentures contains an "Agreement to Subordinate." The Agreement states:

> each Holder likewise covenants and agrees by his acceptance thereof, that the obligations of the Company to make any payment on account of the principal of and interest on each and all of the Notes shall be subordinate and junior, to the extent and in the manner hereinafter set forth, in right of payment to the Company's obligations to the holders of Senior indebtedness of the Company.[1]

The Indentures also specifically acknowledge the priority rights of the Senior Debt holders in the event of bankruptcy.

> The Company agrees that upon . . . any payment or distribution of assets of the Company of any kind or character, whether in cash, property or securities, to creditors upon any dissolution or winding up or total or partial liquidation or reorganization

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1. The quoted text is from the Floating Rate note. The other two notes are materially identical.

> of the Company, whether voluntary or involuntary or in bankruptcy, insolvency, receivership, conservatorship or other proceedings, all principal (and premium, if any) sinking fund payments *and interest due or to become due upon all Senior Indebtedness of the Company shall first be paid in full*, or payment thereof provided for in money or money's worth in accordance with its terms, before any payment is made on account of the principal of or interest on the indebtedness evidence by the [Junior] Notes due and owing at the time. . . .

(Emphasis added). The parties agree that the Senior Debt holders are first in line for the payment of principal and pre-petition interest. The only dispute is over post-petition interest.

BNEC declared bankruptcy in 1991. The Trustee of BNEC's estate, Dr. Ben Branch, having done a truly remarkable job of marshaling BNEC's assets, has paid the principal of the Senior Debt in full, together with all pre-petition interest, post-petition fees, and the Senior Debt holders' expenses.[2] On May 23, 2001, the Trustee sought permission from the Bankruptcy Court to distribute $11,000,000 from BNEC's estate to the Junior Debt holders. The Senior Debt holders objected, claiming priority entitlement to post-petition interest. On November 1, 2001, Chief Bankruptcy Judge William Hillman authorized the

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2. The Trustee has also established a reserve to pay any future legal fees and expenses of the Senior Debt holders.

distribution. In a written opinion, Judge Hillman held that the language of the Junior Debt Indentures guaranteeing the Senior Debt holders "payment in full" of "interest . . . due and owing" did not include post-petition interest. This appeal ensued.

At the hearing before the district court, the parties agreed that *de novo* review of Judge Hillman's Order is called for as there are no disputes of fact and the operative language of the Indentures is (at least in the eye of the beholder) unambiguous. *See In re Winthrop Old Farm Nurseries, Inc.*, 50 F.3d 72, 73 (1st Cir. 1995) (a district court is to review *de novo* a Bankruptcy Court's conclusions of law). If the court were, however, to conclude that Judge Hillman's decision was based on ambiguities in the language of the subordination agreement, the Junior Debt holders maintain that the "clearly erroneous" standard should be applied instead. While

> [t]he interpretation of a contract is generally a question of law and subject to . . . *de novo* review," *Network Pub. Corp. v. Shapiro*, 895 F.2d 97, 99 (2d Cir. 1990), this general proposition applies only when the language of the contracts is unambiguous. *Rothenberg v. Lincoln Farm Camp, Inc.*, 755 F.2d 1017, 1019 (2d Cir. 1985). When the language of the contract is susceptible to more than one reasonable interpretation, the interpretation of the contract is an issue of fact.

In re The Brunswick Hosp. Ctr., Inc., 156 B.R. 896, 899 (E.D.N.Y. 1993). Because I do not interpret Judge Hillman's decision to be based on any perceived ambiguity in the

language of the Indentures, but rather on his legal conclusion that the language used failed to satisfy the Rule of Explicitness, the *de novo* standard of review applies.[3]

The genesis of the dispute on appeal arises from the interplay between two seemingly contradictory provisions of the Bankruptcy Code. Under 11 U.S.C. § 502(b)(2), a creditor in a bankruptcy proceeding is not entitled to post-petition interest.

> (b) Except as provided . . . the court, after notice and a hearing, shall determine the amount of [a bankruptcy] claim in lawful currency of the United States as of the date of the filing of the petition, . . . except to the extent that—. . .
>
> (2) such claim is for unmatured interest.

Under 11 U.S.C. § 510(a), which was inserted into the Bankruptcy Code by Congress in 1978, "[a] subordination agreement is enforceable in a case under this title to the same extent that such agreement is enforceable under applicable nonbankruptcy law."

The enactment of section 510(a) precipitated a debate over whether Congress had intended to abrogate the equitable foundation on which the Bankruptcy Court had erected the

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3. The Rule of Explicitness "prevents a senior creditor from recovering post-petition interest from junior creditors unless the subordination agreement articulates the obligation in unusually express language." *In re Southeast Banking Corp.*, 156 F.3d 1114, 1118 (11th Cir. 1998) (*Southeast Banking I*).

Appendix B

Rule of Explicitness. The origins of the Rule are ably explained in *Southeast Banking I.*

> The overriding theme of bankruptcy law, both past and present, has been the equitable distribution of the debtor's remaining assets among creditors. . . . The courts, however, have permitted creditors to contract out of this system of pro-rata distribution by enforcing subordination agreements, whereby one creditor (the junior creditor) agrees that, in the event of a default or bankruptcy, another creditor (the senior creditor) will receive repayment in full before the junior creditor receives payment on its loans. . . . In enforcing subordination agreements, however, the courts have emphasized that the junior creditor's agreement to subordinate must be express. *See In re Credit Industrial Corp.*, 366 F.2d at 408.
>
> The issue of post-petition interest has led to a wrinkle in the enforcement and interpretation of subordination agreements. Given the often lengthy delay between the debtor's petition for bankruptcy and the date upon which a creditor can expect to receive any payment on the underlying obligation, post-petition interest can represent a significant amount of money. Under both pre-Code practice and the 1978 Bankruptcy Code, unsecured and undersecured creditors could not expect to receive interest on a bankrupt debtor's obligation that accrued after the date of the bankruptcy petition—

at least not from an insolvent debtor. *See* 11 U.S.C. § 502(b)(2) (instructing courts to determine the amount of a creditor's claim on the date of the petition and disallowing claims for "unmatured interest").

. . .

In a number of cases, senior creditors sought to avoid this result and recover post-petition interest—not from the debtor, but from the distributions made to junior creditors subject to subordination agreements. Citing the junior creditors' agreement to subordinate their right to repayment until the senior debt had been paid in full, senior creditors argued that even though bankruptcy law prevented their recovery of post-petition interest from the debtor, their loans had not been paid in full and, therefore, that they could demand payment from whatever distribution the junior creditors received from the debtor. In 1974, before Congress adopted the Bankruptcy Code, the Court of Appeals for the Third Circuit addressed this argument and concluded that a junior creditor could agree to subordinate its claim to a senior creditor's demands for post-petition interest, if the subordination agreement *explicitly* provided for such a result:

> "If a creditor desires to establish a right to post-petition interest and a concomitant reduction in the dividends due to

> subordinated creditors, the agreement should clearly show that the general rule that interest stops on the date of the filing of the petition is to be suspended, at least vis-a-vis these parties."
>
> *In re Time Sales Fin. Corp.*, 491 F.2d 841, 844 (3d Cir. 1974).

> Significantly, however, the *Time Sales* court held that general language in the subordination agreement, establishing that the senior debt must be "paid in full" before payment on the junior debt, was insufficient to alert the junior creditor that it had agreed to subordinate its claims to the senior creditor's claims for post-petition interest. . . . A number of courts, when confronted with similar claims and subordination agreements, adopted the Third Circuit's approach and dubbed it the "Rule of Explicitness."

Id. at 1118-1120.

Ultimately, the Court in *Southeast Banking I* concluded that the enactment of section 510(a) had indeed abrogated the Rule "as the progeny of the bankruptcy courts' equity powers or as a federal canon of contract construction." *Id.*, 156 F.3d at 1124. To the extent that the Rule survived section 510(a), it do so only as a matter of State law.

> The language of section 510(a) . . . directs courts to enforce subordination agreements to the extent

> that the agreements are enforceable under "applicable nonbankruptcy law." 11 U.S.C. § 510(a). In another context, the Supreme Court has held that Congress's use of the phrase "applicable nonbankruptcy law" in the Bankruptcy Code refers to any relevant federal or state law. *See Patterson v. Shumate*, 504 U.S. 753, 757-759 (1992) (noting that nonbankruptcy law is broader than state law, a term Congress also used in the Bankruptcy Code). Unlike the *Patterson* case, which involved a relevant provision of federal legislation, however, the parties before us have identified no independent federal statute that might guide the interpretation of subordination agreements; nor have they argued that federal common law should govern the outcome of this case. This absence of relevant federal authority should not be surprising because the enforcement and "interpretation of private contracts is ordinarily a question of state law.") *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 60 n. 4 (1995) (quoting *Volt Info. Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 474 (1989)); *see also Butner v. United States*, 440 U.S. 48, 55 (1979) ("Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.").

Id. at 1121. (Extended citations and footnote omitted).

Appendix B

The Indenture at issue in *Southeast Banking I*, as here, contained a New York choice of law clause. "Since our review of New York law revealed no intimation of what specific language (if any) the New York courts would require to put a junior creditor on notice regarding the significant risk of subordinating a debt to a senior creditor's claims for post-petition interest and post-petition fees and costs, we CERTIFIED this important question to the New York Court of Appeals." *Id.*, 156 F.3d at 1125-1126.[4]

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4. The precise question asked was: "What, if any, language does New York law require in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of the senior creditor's post-petition interest?" *Id.*, 156 F.3d at 1125. One could argue that the question was the wrong one, and that what the Court meant to ask was not how the New York Court of Appeals defined the Rule of Explicitness, but whether it recognized the Rule at all. As the Eleventh Circuit noted earlier in *Southeast Banking I*, the contours of the Rule were well-established. Indeed, given the consensus achieved by the Rule, the Eleventh Circuit wondered "whether the New York courts would disturb the heretofore uniform treatment of this question, particularly given the evidence that the capital markets appear to have adjusted to the Rule of Explicitness." *Id.* at 1124. "Nevertheless," the Court continued, "since this is an important question of first impression for the New York courts, . . . we are reluctant to predict its resolution under New York law." *Id.* at 1125. Certainly, the Court of Appeals gave more attention to the second question than it did to the actual question asked by the Eleventh Circuit. The Court of Appeals introduced its discussion with the prefatory remark that "we [now] face up to whether New York should adopt [the Eleventh Circuit's] version of the Rule of Explicitness as a guiding interpretive principle of State contract dispute resolution in cases such as this." *In the Matter of Southeast Banking Corp.*, 93 N.Y.2d 178, 183 (1999).

Appendix B

The New York Court of Appeals answered as follows: "In accordance with the Rule of Explicitness, New York law would require specific language in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of allowing the payment of a senior creditor's post-petition interest demand." *In the Matter of Southeast Banking Corp.*, 93 N.Y.2d at 186. This answer led the Eleventh Circuit to reaffirm its prior determination that "we find it beyond question that the subordination language in the indenture agreements in this case, which requires 'payment in full' without any specific reference to post-petition interest, is insufficiently 'precise, explicit and unambiguous' on the topic of post-petition interest to satisfy the Rule of Explicitness." *In re Southeast Banking Corp. II*, 179 F.3d 1307, 1310 (11th Cir. 1999).

The Junior Debt holders argue that on the basis of this exchange, it is clear that for a claim to post-petition interest to survive the Rule of Explicitness, a subordination agreement must specifically reference the entitlement of the Senior Debt holders to such interest. I agree.[5] There is nothing ambiguous about the word "explicit." It means "fully and clearly expressed or demonstrated; leaving nothing merely implied." *Random House Unabridged Dictionary; Second Edition* (1993). This is especially the case when one is dealing with a bankruptcy term of art like "post-petition interest,"

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5. The Senior Debt holders make a convoluted, clever, and ultimately unconvincing argument that the Court of Appeals never really answered the certified question but simply deferred to the Eleventh Circuit's determination that the language in the subordination agreement at issue (which was virtually identical to the language in this case) failed to satisfy the Rule of Explicitness.

whose meaning would not be apparent to an ordinary investor unschooled in bankruptcy law, much less thought to be comprehended in a terms as general as "payment in full" or "due and owing."[6]

ORDER

For the foregoing reasons, the Order of the Bankruptcy Court is *AFFIRMED.*

SO ORDERED.

s/ Richard G. Stearns
UNITED STATES DISTRICT JUDGE

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6. The Senior Debt holders argue that the phrase "interest due or to become due" can only refer to post-petition interest as it is the only interest that could "become due" after a bankruptcy (because post-petition interest is otherwise disallowed). While the argument is not devoid of logic, it is not explicit, but depends on inferences drawn from the judicial reconciliation of the conflict between section 502(b)(2) and section 510(a).

APPENDIX C — MEMORANDUM DECISION ON TRUSTEE'S MOTION FOR ORDER AUTHORIZING FOURTH INTERIM DISTRIBUTION OF THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF MASSACHUSETTS DATED NOVEMBER 1, 2001

UNITED STATES BANKRUPTCY COURT
for the
DISTRICT OF MASSACHUSETTS

Chapter 7

No. 91-10126-WCH

In re:

BANK OF NEW ENGLAND CORPORATION,

Debtor

MEMORANDUM DECISION ON TRUSTEE'S MOTION FOR ORDER AUTHORIZING FOURTH INTERIM DISTRIBUTION

Dr. Ben S. Branch, Chapter 7 Trustee (the "Trustee") of Bank of New England Corporation ("BNEC" or "the Company") has moved for authority to make a fourth interim distribution in the amount of $11,000,000 to the creditors of the estate (the "Motion"). As to the recipients of this distribution, the Trustee avers:

> Pursuant to the contractual subordination provisions of BNEC's indentures, the Senior Bondholders have been paid in full. Accordingly,

> on the date of the Fourth Interim Distribution, all payments to which the holders of senior indebtedness would be entitled shall be paid to the Junior Indenture Trustees for distribution to the holders of BNEC's subordinated indebtedness.

Motion, ¶ 16.

HSBC Bank USA, as successor to Marine Midland Bank, N.A., and The Chase Manhattan Bank, as successor to Manufacturers Hanover Trust Company (collectively, the "Senior Indenture Trustees") filed an objection to the proposed distribution. U.S. Bank Trust National Association and Chemical Bank Delaware (collectively, the "Junior Indentures Trustees") joined in support of the Motion. After a hearing I took the matter under advisement and I now grant the Motion. The following constitute my findings of fact and conclusions of law in accordance with Fed. R. Bankr. P. 7052.

Facts

There are no substantive factual issues to be resolved; it is the application of the law to the undisputed facts which is in controversy. This recitation is derived primarily from the *Trustee's Reply Brief Supporting Motion for Order Authorizing Fourth Interim Distribution.*

BNEC filed this Chapter 7 case over ten years ago. Prior to filing, BNEC had issued six separate issues of indenture debt, aggregating $705,972,000 in principal amount. Three issues are entitled to the benefit of contractual subordination provisions, and will be described as the Senior

Debt. The remaining three issues (the "Junior Debt") contractually subordinate payment in accordance with the terms of their indentures (the "Junior Indentures").

Through prior interim distributions, the Trustee has paid to the Senior Debt all allowed claims for principal and pre-petition interest plus post-petition fees and expenses incurred through the date of the last such distribution. The Trustee has created a reserve to cover any future fees and legal expenses. He proposes to make the next interim distribution to the Junior Debt. In the Objection, the Senior Indenture Trustees assert that the distribution should be first applied to post-petition interest due on the Senior Debt.

Each of the Junior Indentures provides that it is governed by New York law and contains a provision virtually identical to the following, which is quoted from one such indenture:

> [E]ach Holder likewise covenants and agrees by his acceptance thereof, that the obligations of the Company to make payment on account of the principal and interest on each and all of the Notes shall be subordinate and junior, *to the extent and in the manner hereinafter set forth*, in right of payment to the Company's obligations to the holders of Senior Indebtedness of the Company. (emphasis added).

The "extent and manner hereinafter set forth" includes the following provision:

> The Company agrees that upon . . . any payment or distribution of assets of the Company of any

> kind or character, whether in cash, property or securities, to creditors upon any dissolution or winding up or total or partial liquidation or reorganization of the Company, whether voluntary or involuntary or in bankruptcy, insolvency, receivership, conservatorship or other proceedings, all principal (and premium, if any), sinking fund payments and interest due on or to become due upon all Senior Indebtedness of the Company *shall first be paid in full*, or payment thereof provided for in money or money's worth in accordance with its terms, before any payment is made on account of the principal or interest on the indebtedness evidenced by the [Junior] Notes due and owning at the time. . . . (emphasis added).

Issue

The issue before me resolves itself into the meaning of the emphasized phrase "shall first be paid in full." If that language does not encompass post-petition interest, the Trustee's position is well taken and the present motion should be granted as presented. If it does have the added breadth, then the interim distribution should be authorized (no one disputes this) but payment would go to the Senior Indenture Trustees to the extent of post-petition interest, which appears to far exceed the amount proposed for distribution.

Discussion

The outcome of this controversy will depend upon the application of the so-called Rule of Explicitness to the

language used in the Junior Indentures. That principle is generally traced to *Bankers Life Co. v. Manufacturers Hanover Trust Co. (In re Kingsboro Mortgage Corp.)*, 514 F.2d 400 (2d Cir. 1975), where the issue was the same as now before me. The language before the court in that case was strikingly similar to that quoted above:

> In the event of any insolvency, bankruptcy liquidation, reorganization or other similar proceedings . . . then all principal and interest on all Senior Debt *shall first be paid in full* . . . before any payment on account of principal or interest is made upon the Notes (junior indebtedness).

514 F.2d at 401 (emphasis added).

The Court of Appeals held that the quoted language "is insufficiently express to relate to post-bankruptcy interest." *Id. See also In re Time Sales Fin. Corp.*, 491 F.2d 841, 844 (3d Cir. 1974) ("If a creditor desires to establish a right to post-petition interest and a concomitant reduction in the dividends due to subordinated creditors, the agreement should clearly show that the general rule that interest stops on the date of the filing of the petition is to be suspended, at least vis-a-vis these parties.")

At that time, of course, the operative law was the Bankruptcy Act, but its § 63(a)(1),[1] like the present law's

1. "Debts of the bankrupt may be proved and allowed against his estate which are founded upon (1) a fixed liability, as evidence by a judgment or an instrument in writing, absolutely owing at the (Cont'd)

§ 502(b)(2),[2] denied creditors post-petition interest. Missing from the Act, however, was a provision comparable to the Bankruptcy Code's § 510(a): "A subordination agreement is enforceable in a case under this title to the same extent that such agreement is enforceable under applicable nonbankruptcy law."

The addition of § 510(a) led to a debate as to whether the Rule of Explicitness had been overruled. A scholarly examination of that issue can be found in *Chemical Bank v. First Trust of New York (In re Southeast Banking Corp.)*, 156 F.3d 1114 (11th Cir. 1998). Finding itself in doubt, the Eleventh Circuit certified the following question to the New York Court of Appeals:

> What, if any, language does New York law require in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of the senior creditor's post-petition interest?

Id. at 1125.

(Cont'd)
time of the filing of the petition by or against him, whether then payable or not, with any interest thereon which would have been recoverable at that date. . . ." 11 U.S.C. § 63a (Repealed).

2. (b) Except as provided in subsections (e)(2), (f), (g), (h) and (i) of this section, if such objection to a claim is made, the court, after notice and a hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that . . . (2) such claim is for unmatured interest. . . ." 11 U.S.C. § 502(b)(2).

Appendix C

The New York Court of Appeals responded that

> In accordance with the Rule of Explicitness, New York law would require specific language in a subordination agreement to alert a junior creditor to its assumption of the risk and burden of allowing the payment of a senior creditor's post-petition interest demand.

Chemical Bank v. First Trust of New York (In re Southeast Banking Corp.), 93 N.Y.2d 178, 186, 710 N.E.2d 1083, 1088 (1999).

The Senior Indenture Trustees oppose application of the stated principle to the present case. They argue that the New York Court of Appeals decision was based upon that conclusion of the Eleventh Circuit that "paid in full" was ambiguous, and that, based upon non-bankruptcy New York precedents, the term would require payment of interest until the date of the payment of all principal. *Objection*, ¶ 17. They further urge that the words "due or to become due" satisfy the New York law requirement for specific language. *Objection*, ¶ *18*. I am not persuaded by either argument.

As to the former, the Senior Indenture Trustees stop short of the actual reasoning of the New York Court of Appeals. While it noted the "binding threshold ruling" of the Eleventh Circuit that "paid in full" is ambiguous in the context of the pertinent subordination agreements, 688 N.Y.2d at 486, 710 N.E.2d at 1085, it continued:

> For the purposes of answering the particular question posed to us, we are confined by key

> features of the Eleventh Circuit's ruling. Nevertheless, we face up to whether New York should adopt its version of the Rule of Explicitness as a guiding interpretive principle of State contract dispute resolution in cases such as this.

Ibid.

It is in the latter context—establishment of a general principle of state law—that the court spoke.

As to the latter argument, the imposition of bankruptcy truncates the power of the contractual "due or to become due" phrase. Interest will no longer become due. 11 U.S.C. § 502(b)(2).

An order will enter granting the Motion.

s/ William C. Hillman
William C. Hillman
Chief Judge

Dated: 11/01/01

APPENDIX D — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT DENYING PETITION FOR REHEARING ENTERED MAY 5, 2004

UNITED STATES COURT OF APPEALS
For the First Circuit

No. 0-1321

IN RE: THE BANK OF
NEW ENGLAND CORPORATION

Debtor

HSBC BANK USA, as Indenture Trustee;
JP MORGAN CHASE BANK,
f/k/a Chase Manhattan Bank, N.A.

Appellants,

v.

THE BANK OF NEW ENGLAND CORPORATION;
CHEMICAL BANK DELAWARE;
US BANK TRUST NATIONAL ASSOCIATION;
DR. BEN S. BRANCH, Trustee

Appellees.

Before

Boudin, *Chief Judge*,
Coffin, *Senior Circuit Judge*,
Torruella* and Selya, *Circuit Judges*,
Lynch, Lipez and Howard *Circuit Judo*,
William E. Smith**, *District Judge*.

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* Judge Torruella is recused and did not participate in the consideration of this matter.

** Of the District Of Rhode Island, sitting be designation.

Appendix D

ORDER OF COURT
Entered: May 5, 2004

The panel of judges that rendered the decision in this case having voted to deny the petition for rehearing and the suggestion for rehearing en banc having been carefully considered by the judges of the Court in regular active service and a majority of said judges not having voted to order that the appeals be heard or reheard by the Court en banc,

It is ordered that the petition for rehearing and the suggestion for rehearing en banc, be *denied*.

By the Court:
RICHARD CUSHING DONOVAN, Clerk

By: s/ MARK R. SYSKA
Chief Deputy Clerk.